Edexcel (B) Economics A-level

Theme 2.2: Firms, Consumers and Elasticities of Demand

Flashcards

Define and give the formula for Price Elasticity of Demand

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PED is the responsiveness of quantity demanded given a change in price

PED= Δ%QD / Δ%P

If PED is less than 1, will QD move to a larger or smaller degree than price?

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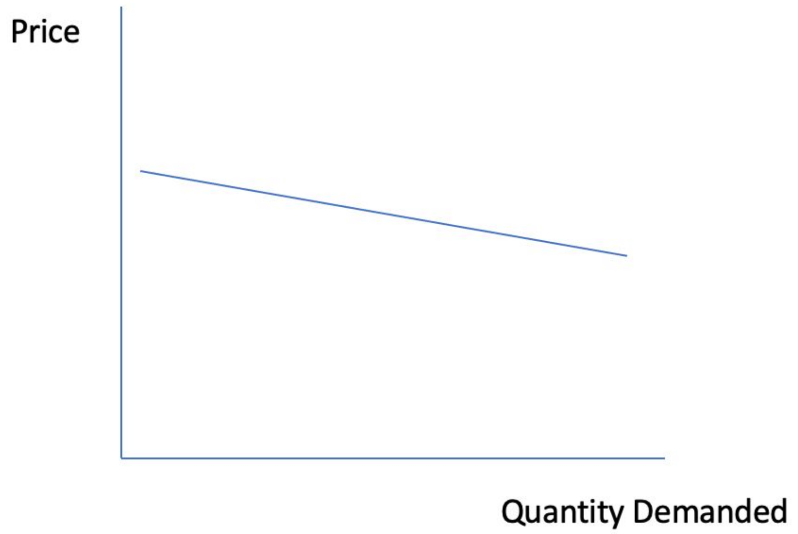
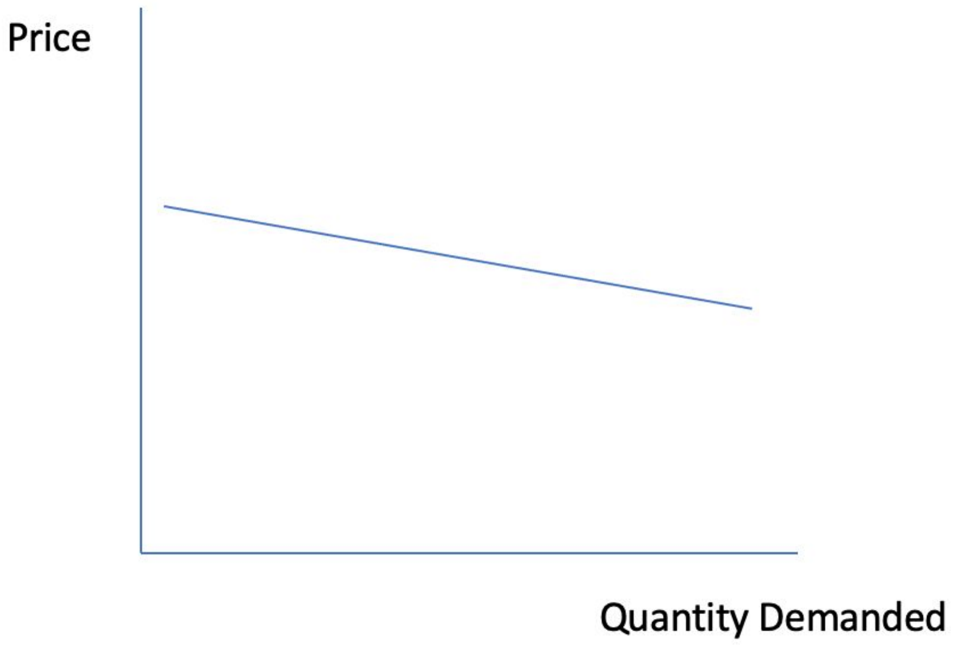
A change in price will lead to a smaller change in the level of quantity demanded

Does this graph represent a PED elastic or inelastic good?



Does this graph represent a PED elastic or inelastic good?

PED elastic good



What does PED = 1 represent?

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A unitary elastic good, whereby the change in price is equal to the change in quantity demanded

Draw the graph for a perfectly inelastic good

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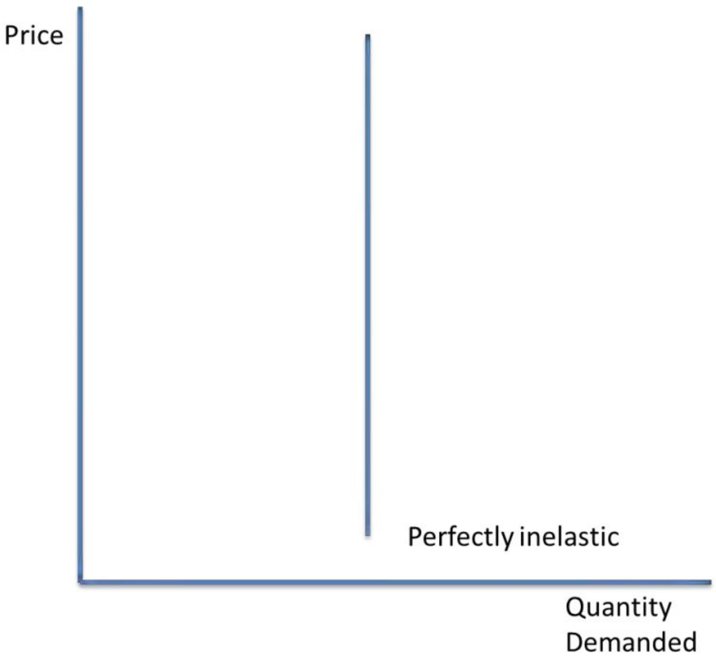

If price increased by 22% and quantity demanded decreased by 30%, is the good PED elastic or inelastic?

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-30 / 22 = -1.36

Therefore a PED elastic good

Name the 6 factors influencing elasticity of demand

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1. Necessity
2. Substitutes
3. Habitual consumption
4. Proportion of income spent
5. Durability
6. Peak/off-peak demand

How does the number of substitutes affect the elasticity of demand for the good?

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The more substitutes there are, the more PED elastic the good is

Would peak demand for a good make it PED elastic or inelastic?

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PED inelastic

If good ‘A’ is PED elastic and the price of the good increases, what happens to revenue?

If good ‘A’ is PED elastic and the price of the good increases, what happens to revenue?

The fall in quantity demanded is proportionally larger than the increase in price, so overall revenue falls

Describe the concept of price skimming

PMT
•resources•tuition•courses

Describe the concept of price skimming

A short-term pricing strategy that usually occurs when a new product is released, whereby a high price is set before new firms enter the market and increase competition

How does predatory pricing differ from price penetration?

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Predatory pricing aims to push incumbents out of the market, whereas price penetration aims to boost customer loyalty

List the 3 factors that determine the most appropriate pricing strategy

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1. Number of USPs
2. Price elasticity of demand
3. Stage in the product life cycle

If good ‘A’ has a high PED, will firms give it a high or low price, and why?

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A low price because the good is dependent on price so if the good was expensive, firms’ profit margins would be at risk

Give the formula for income elasticity of demand

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$$YED = \Delta\%QD / \Delta\%Y$$

Define inferior goods and give their YED value

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Goods that experience a reduction in demand as income falls.

YED less than 0

Name the type of good with a YED greater than 1

Name the type of good with a YED greater than 1

Normal luxury goods

During an economic recession, what type of goods are firms more likely to produce, and why?

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Inferior goods, because recessions usually accompany a reduction in income, so inferior goods will experience an increase in demand